Internal Revenue Service

memorandum

CC:TL-N-1782-88
BrlCEButterfield

date: JAN 15 1988

to: District Counsel, Laguna Niguel CC:LN

from: Director, Tax Litigation Division CC:TL

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subject: [redacted]

This responds to your request for technical advice dated December 4, 1987.

ISSUE

Whether any attorneys' fees should be offered to the taxpayer as part of the stipulated dismissal of the above-captioned case. RIRA No. 7430.00-00

CONCLUSION

The government's conduct of this case was substantially justified, and does not warrant the award of costs or attorneys' fees.

FACTS

A statutory notice of deficiency was issued to the taxpayers on [redacted], for their [redacted] and [redacted] taxable years. The notice disallowed a partnership loss deduction for the [redacted] year, and the related carryback to the [redacted] year. Although the years subject to the notice had not been examined, the same issue was the subject of an examination for the [redacted] and [redacted] tax years. The taxpayer had not extended the statute of limitations for [redacted], and the statute was about to expire, so the notice of deficiency was issued. The notice was issued based on the petitioner's return for the [redacted] year.

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Taxpayer filed a petition on [redacted], which was answered [redacted]. After the filing of the answer petitioner's counsel produced a "no change" letter dated [redacted], seven months after the notice, which applied to all the years involving the partnership deductions through [redacted]. Subsequently, District Counsel agreed to concede the case, with the final stipulation to be filed after resolution of the informal request regarding attorneys' fees. According to section (n) of the petition, subsequent to the issuance of the notice of deficiency, the Service began collection activities. This allegation is denied in the answer, and no information supporting it is contained in the file.

LEGAL ANALYSIS

The petition in this case was filed after December 31, 1985. Therefore, section 7430, as amended by section 1551 of the Tax Reform Act of 1986, allows the court to award fees and costs to petitioners who have substantially prevailed in civil actions under the Code, where the government's litigating position was not substantially justified, and where the petitioner exhausted administrative remedies before filing the petition.

In this case administrative remedies would be deemed to have been exhausted under Treas. Reg. § 301.7430-1(f)(3)(ii). Also, because the government is conceding the case, we do not dispute that petitioner has substantially prevailed. However, we believe that the actions of the government in litigating this case were substantially justifiable, and that no award of fees or costs is warranted.

Because your discussion with opposing counsel is being carried out at an informal level, we do not have the benefit of a motion for fees and itemized billing, to clarify what expenditures petitioner feels are recompensable, or at what rate. Any award related to activity prior to the filing of the petition, or related to the abatement of collection activity after such filing, would not be recoverable under any circumstances. Section 7430 is a waiver of sovereign immunity. It must therefore be strictly construed. Ruckelshaus v. Sierra Club, 463 U.S. 680 (1983); Ewing and Thomas, P.A. v. Heye, 803 F.2d 613 (11th Cir. 1986). The statute authorizes fees and costs for actions (or inaction) by the District Counsel attorney. It makes no provision for costs incurred in administrative matters, whether or not the administrative actions of the agency were substantially justifiable, as long as the District Counsel attorney had no involvement in them. Sher v. Commissioner, 89 T.C. No. 9 (July 9, 1987).

At issue then is whether the litigating position of the government was substantially justifiable in this case. The litigating position of the government consisted of a standard

answer, followed by full concession once the no change letterhad been generated and brought to the attorney's attention. Stipulated dismissal is a fully reasonable response to the facts of this case. Shifman v. Commissioner, T.C.M. 1987-347. A related question which must be addressed is whether the decision to concede was made in a reasonable amount of time. The court in Rouffy v. Commissioner, T.C.M. 1987-5, likewise considering only the post-petition actions by the government, found that concession after six months, based on an investigation that was begun promptly, did not justify an award of attorneys' fees.

Several other cases have supported our litigating position that the Tax Court only has jurisdiction to make an award of attorneys' fees based on the post-petition action or inaction of the Service. Sher v. Commissioner, 89 T.C. No. 9 (July 9, 1987); Weiss v. Commissioner, 89 T.C. No. 54 (October 8, 1987); Stieha v. Commissioner, 89 T.C. No. 55 (October 8, 1987). In this case the no change letter was not generated until after the petition was filed, and once it was presented to the District Counsel attorney an agreement to concede was reached in a reasonable time. The notice of deficiency in this case was not based on a full audit of the tax years in question, but was issued in the face of an expiring statute of limitations. A protective notice issued with reference to the return of the individual, correctly referring to the partnership loss, and the amount of deficiency is not of the type found to be invalid in Scar v. Commissioner, 814 F.2d 1363 (9th Cir. 1987). Therefore we do not believe that a court would hold that our position after the petition was filed was not substantially justifiable on that basis either.

We do believe that our position that the administrative basis for litigation may not be considered in making a determination of substantial justifiability is subject to some litigation hazards. Several cases under the pre-1986 version of section 7430 found that pre-petition administrative action could be considered in this determination. Kaufman v. Egger, 758 F.2d 1 (1st Cir. 1985); Powell v. Commissioner, 791 F.2d 385 (5th CIr. 1986). This line of reasoning might be reopened by the Circuits for post-1986 cases. However, on the facts of this case we believe that even the pre-petition activity by the Service was substantially justifiable. It is Service position that it can issue notices of deficiency under the circumstances pertaining here. In litigation the courts have been reluctant to find notices of deficiency invalid (with the notable exception of Scar, which we believe does not apply to this case). Estate of Brimm v. Commissioner, 70 T.C. 15 (1978); Greenberg's Express, Inc. v. Commissioner, 62 T.C. 324 (1974). Therefore, even the broader view of what may be considered to determine whether the position of the government was substantially justifiable would not result in an award of fees in this case.

Although the final outcome will be full concession by the government, the attorneys' fees provision was never intended to result in an award of fees every time a party prevails against the Commissioner. Only when the government cannot justify its post-petition actions under the standards described above is an award authorized, and we do not believe that this is such a case. If you have any questions with regard to this matter, please do not hesitate to call Ms. Clare E. Butterfield, at (FTS) 566-3442.

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